COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of

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| NOTICE OF SOUTH CENTRAL BELL TELEPHONE COMPANY OF AN ADJUSTMENT IN ITS INTRASTATE RATES AND CHARGES | ) | CASE NO. 8150 |

# ORDER

On December 4, 1981, South Central Bell Telephone Company ("Bell") filed with the Commission, in compliance with the Commission's order in this case dated August 11, 1981 ("August order"), its tariffs to recover expense increases resulting from the second year of the 4-year phase-in for the expensing of station connections; the revised lives and salvage rates agreed to in the September 8-11, 1981, "Three-Way" meeting; and the use of remaining life depreciation. The Commission allowed Bell to place these tariffs into effect on January 1, 1982, subject to refund, pending the outcome of a hearing and investigation by the Commission pursuant to a petition for hearing filed by the Consumer Protection Division of the Attorney General's Office ("AG").

## Absorption

Bell and the AG, through their respective expert witnesses, filed conflicting testimony concerning Bell's ability to absorb these increased expenses. The differences of opinion are due to different interpretations of the absorption criteria in the Commission's August order.

In its August order the Commission allowed Bell to file tariffs to recover the additional expenses incurred through the phasing-in of expensing station connections. The Commission further stated on page 20 of the August order that, to be eligible for the full revenue requirements from the additional expensing, Bell had to meet a strict absorption test stated as follows:

> Bell must, moreover, demonstrate, based on actual results adjusted solely for the effect of rate increases, that absorption of these increased costs would result in Bell not achieving the return on equity allowed in this order.

Interpreting this statement to mean that Bell could not adjust its expenses in any manner, the AG demonstrated Bell's ability to absorb a portion of the increase in expenses when leaving expenses at the actual 1981 level. Bell objected to this interpretation of the Commission's statement since it had made adjustments to expenses for known changes approved in the August order in its general rate case. Moreover, Bell contended that it is inconsistent to require an adjustment to reflect the increase in revenues resulting from a rate case, while not permitting adjustments to expenses on which the Commission had based its decision regarding the amount of increase.

The Commission agrees with Bell in this interpretation. However, in future annual periods not affected by a general rate case no adjustments to expenses shall be allowed, but revenues must be adjusted to reflect changes such as increases from regroupings and the annualized effect of new service offerings.

The AG, moreover, interpreted the Commission's statement to mean that the return on equity should be computed without the inclusion of accumulated deferred job development investment tax credits ("JDIC"), and that the range of equity returns should apply in the absorption test, rather than the return on which the Commission based its rate case findings on revenue requirements. Bell objected to both interpretations.

The Commission cannot exclude JDIC in its calculation of return without subjecting Bell to the potential loss of the credit under federal law. Since it would be detrimental to the ratepayers for Bell to lose this credit, the Commission will not establish any standard which might jeopardize the credit. As to the issue of whether the range of returns or the actual return found fair, just and reasonable should be used in the application of the absorption test, it is the opinion of the Commission that the return used to compute revenue requirements is the appropriate standard for purposes of this test.

Based on the foregoing analysis the Commission concludes that Bell has demonstrated its inability to absorb any portion of the increased expenses referred to above.

## RATE DESIGN

In its original application in this case, Bell requested rate adjustments that included revenue requirements resulting from the expensing of station connections, the revised depreciation schedule, and the adoption of remaining life depreciation methodology. Rates associated with the expensing of station connections were identifiable as a specific rate component or readily attributable to a specific category of rates.

Upon final determination of revenue requirements in its August Order, the Commission made adjustments to requested rates in the areas of service charges, telephone sets and adjuncts, private line, and local service rates. Service charges were adjusted to effect the Commission's adoption of a 4-year phase-in period for the expensing of station connections. Rates requested for private line were denied as a result of Commission action in other cases. Telephone sets and adjuncts and local service rates were adjusted to reflect the Commission's deferral of depreciation issue.

In the current application, the Commission authorized increased service charges to reflect the second year of the phase-in of the expensing of station connections. In addition, the Commission authorized increased charges for telephone sets and adjuncts, for increased depreciation expense resulting from revised depreciation schedules and the use of remaining life depreciation methodology.

IT IS THEREFORE ORDERED that the AG's Petition for Hearing filed December 22, 1981, be and it hereby is denied.

IT IS FURTHER ORDERED that the tariffs approved by the Commission on January 4, 1982, subject to refund, are the fair, just and reasonable rates for Bell to charge its customers and should remain in full force and effect.

Done at Frankfort, Kentucky, this 5th day of May, 1982.

PUBLIC SERVICE COMMISSION

Chairman

Vice Chairman

Commissioner

ATTEST:

Secretary